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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Price Cap Performance Review	)	CC Docket No. 94-1
for Local Exchange Carriers	)	

COMMENTS OF THE

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COMMENTS OF THE CALIFORNIA CABLE TELEVISION ASSOCIATION

The California Cable Television Association ("CCTA") hereby submits its comments on the Commission's Second Further Notice of Proposed Rulemaking[1/] in the above-referenced docket regarding the price cap performance review for local exchange carriers of telecommunications services ("LECs"). CCTA is a trade association representing cable television operators with over 400 cable television systems in California, including both small and rural systems and national multiple system operators. Its members are currently planning to compete with the LECs in California as facilities-based providers of local telephone service (including exchange and exchange access service) to residential and business consumers throughout California.[2/]

[1/] In the Matter of Price Cap Performance Review for Local Exchange Carriers, Second Further Notice of Proposed Rulemaking in CC Docket No. 94-1, FCC 95-393 (rel. September 20, 1995) ("Second Further Notice").

[2/] CCTA has participated actively in the Commission's price caps docket, filing comments and reply comments on the Commission's Notice of Proposed Rulemaking. See, e.g., Comments of CCTA, CC Docket No. 94-1, filed May 9, 1994, Reply Comments of CCTA, filed June 29, 1994.

INTRODUCTION AND SUMMARY

In the Second Further Notice, the Commission seeks comment on proposed changes to interstate access price regulation "to respond to changes in the market for these services and to rely more heavily on market forces to achieve our public policy goals."[3] As a rationale for the proposed changes, the Commission states that "although we recently found in the First Report and Order in CC Docket No. 94-1 that LECs retain considerable market power, we also took notice of the growing evidence that an increasing variety of local telecommunications services are available on a competitive basis."[4] Based upon "these signs of changing market structure," and despite the acknowledged "considerable market power" of the LECs, the Commission proposes to make a multitude of small and large scale adjustments and revisions to the price cap plan it originally adopted in 1990,[5] and which it has systematically refined several times over the years.[6]

The cumulative effect of the changes proposed in the Second Further Notice would be to afford incumbent LECs subject to price cap regulation an unprecedented and dangerous degree of pricing flexibility and freedom from regulatory oversight, with no concrete offsetting public interest benefits. While CCTA acknowledges that there is a developing

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[3] Second Further Notice at ¶ 1.

[4] Id. at ¶ 5.

[5] Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, 5 FCC Rcd. 6786 (1990) ("LEC Price Cap Order"), recon., 6 FCC Rcd. 2637 (1991) ("LEC Price Cap Reconsideration Order"). aff'd sub. nom., National Rural Telecom Assoc. v. FCC, 988 F.2d 174 (D.C. Cir. 1993).

[6] See In the Matter of Price Cap Performance Review for Local Exchange Carriers, First Report and Order, 10 FCC Rcd. 8962 (1995) ("First Report and Order"); see also Transport Rate Structure and Pricing, 10 FCC Rcd. 3030 (1994).

trend toward opening up local telecommunications markets and removing competitive barriers, CCTA asserts that the goal of a competitive local marketplace with robust facilities-based competition has yet to be achieved, and in fact still is several years away. Thus, the cumulative effect that the changes proposed by the Commission could have on consumers and the LECs' competitors could be devastating.

The Commission's proposed adjustments to the LECs' regulatory structure could lead to diminished competition in the local exchange market, ultimately reducing the ability of market forces to promote public policy goals and causing long term harm to consumers by contracting rather than expanding their choices among service providers. In short, instituting the proposed regulatory "relief" for the LECs without a demonstrable showing that there is in fact facilities-based competition for local telecommunications services, could threaten the attainment of the Commission's long-held goal of fostering new and innovative services and markets.

Although there may be an emerging resale market for local telecommunications services today, ultimately resale represents nothing more than the sale of the underlying incumbents' service. While resale is a valuable market extension and conditioning device, it is not a substitute for facilities-based competition, which can at some point in the future obviate the need for some regulation. Today there is no genuine facilities-based competition in local telecommunications markets, which provides the only real basis for meeting the Commission's articulated public interest goals.[7/]

[7/] <u>See</u> fn. 27 <u>infra</u>.

The Commission should not grant regulatory flexibility to the LECs on mere hopes and speculation that a competitive facilities-based market one day will emerge. Instead, it must predicate any relief on an actual demonstration of such competition. In adapting its regulatory policies to the evolving telecommunications marketplace, the Commission must balance the need to afford entrenched LECs justified regulatory flexibility with the critical need to safeguard and promote affirmatively a competitive local telecommunications marketplace.

As the Commission correctly recognized in the Second Further Notice, strong incentives continue to exist which may encourage anticompetitive behavior by the LECs.[8] The Commission must keep these incentives firmly in mind in going forward with any changes to the LECs' price cap formula, particularly when it considers making sweeping, fundamental regulatory changes such as granting the LECs streamlined regulation or nondominant treatment.

If the Commission truly wants to achieve a competitive structure in the local exchange, it must ensure that the timing of increased regulatory flexibility not only is reasoned, but also reasonable. Specifically, the Commission must firmly tie any relaxed regulation of the LECs to the achievement of precise competitive goals, benchmarks, or measures of competition, such as it has with its rules for expanded interconnection.[9]

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[8] Second Further Notice at ¶¶ 19-26, 29.

[9] See Expanded Interconnection with Local Telephone Company Facilities; Amendment of Part 69 Allocation of General Support Facility Costs, 7 FCC Rcd. 7369, 7454 n.411, vacated in part and remanded, Bell Atlantic Tel. Cos. v. FCC, 24 F.3d. 1441 (D.C. Cir. 1994); Expanded Interconnection with Local Telephone Company Facilities, 9 FCC Rcd. 5154, 5196 (1994).

Thus, the Commission should not proceed with increased regulatory flexibility unless and until there is a certification by the LEC that there exists: (1) timely central office interconnection agreements, including cost-effective, seamless interconnection and appropriate billing agreements; (2) nondiscriminatory access to unbundled LEC loops, rights of way, poles, conduit and building access points; (3) timely meet point billing agreements to establish cooperative economic interconnection as part of the physical interconnection process; (4) adoption of the bill and keep compensation methodology until permanent number portability is attained; (5) if bill and keep is not retained after permanent number portability is instituted, there must be fully reciprocal mutual compensation agreements at the LECs' total service long run incremental costs ("TSLRIC"), including for any transit function; (6) equal rights to and control over numbering resources; (7) permanent number portability in every central office; and (8) equal control over network databases through efficient electronic interfaces. In addition, there must be a "fresh look" period of one year for all agreements signed within the previous two years after the LEC certifies that the foregoing conditions are met. And, most importantly, prior to the adoption of any pricing flexibility or similar regulatory relief, there must be a demonstrable showing, as measured by market share, that there exists facilities-based local telecommunications competition.

Because we are still far from a robustly competitive local telecommunications market, and there is no real factual evidence that pricing flexibility is currently justified, the Commission should reject the proposals regarding the alteration of price cap service baskets and the elimination of lower service bands. The risk of anticompetitive behavior remains as strong today as it was eight months ago, when the Commission adopted very limited regulatory flexibility for the LECs. In addition, the Commission should not skew its processes by shortening notice periods, eliminating detailed cost support and shifting the burden of proof for the introduction of new services. If it truly seeks to promote facilities-based competition, the Commission must do so in a balanced, fair manner with its eyes open.

Finally, given the magnitude of the barriers that still exist to the establishment of robust and open facilities-based local telecommunications competition, CCTA believes that any consideration of streamlined regulation and, ultimately, nondominant treatment for the LECs is wholly premature. Indeed, focussing on these mechanisms at the present time serves only to divert the attention and resources of the Commission and all parties from the significant task of balancing regulatory freedom for the LECs with its task to shape and implement rules that remove barriers and establish the existence of facilities-based competition in the local services market.

I. THE COMMISSION SHOULD NOT GRANT PRICE CAP LECS SIGNIFICANT REGULATORY RELIEF UNTIL THERE IS DEMONSTRABLE FACILITIES-BASED COMPETITION

In the Second Further Notice, the Commission acknowledges that an appropriate prerequisite to affording the LECs relaxed regulatory treatment is the development of higher levels of competition in the local services market and the removal of barriers to competitive entry.[10/] Thus, the Commission tentatively concludes that when such a demonstration is made, it is appropriate to grant additional price cap flexibility.[11/] The Commission appears to have reached this tentative conclusion that a showing of the elimination of competitive

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[10/] Second Further Notice at ¶ 106.

[11/] Id. at ¶¶ 106-110.

entry barriers, a less rigorous requirement than a verifiable demonstration of significant facilities-based competition, warrants the proposed regulatory relief because it will enable the LECs to respond to emerging competition.[12] Evidence of actual competition would only be required prior to "streamlining" regulation of the LECs (i.e., removing LEC services from price cap regulation altogether).[13] Accordingly, the Commission sets out and seeks comment on eight criteria that a competitive checklist might include as reasonable indicators that barriers to entry into the local services market have been removed.[14]

CCTA concurs with the Commission that any additional regulatory flexibility for the LECs at this time must be linked directly to the achievement of certain competitive benchmarks. The LECs have enjoyed a great deal of pricing flexibility since the Commission adopted the price cap plan. Indeed, that flexibility only has grown with each successive refinement of the price cap plan since 1990. Yet, the Commission must bear in mind that a loosening of regulatory safeguards must be balanced against the clear goal of facilitating the continued development of meaningful facilities-based competition. Indeed, concern about granting the LECs pricing flexibility without retarding the development of local telecommunications competition played a key role in the design and implementation of the LEC price cap plan in 1990.[15] Now, in view of the broad range of pricing flexibility

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[12] Id. at ¶ 106.

[13] Id.

[14] Included in the Commission's list were: (1) access to unbundled local loops and switches; (2) intrastate expanded interconnection available through contract or tariff; (3) availability of service provider number portability; (4) establishment of mutual compensation arrangements; and (5) intra-LATA toll dialing parity. Second Further Notice at ¶ 108.

[15] See LEC Price Cap Order, 5 FCC Rcd. 6786.

proposed by the Commission, the need for specific measures both to protect and promote the rapid advancement of facilities-based local competition is especially critical.

Thus, despite numerous proceedings and legislative developments in many jurisdictions that have been designed specifically to pave the way for local telecommunications services competition, the fact remains that there are many critical issues that must be addressed and resolved by the creation of rules which must be implemented effectively prior to the realization of facilities-based competition.[16] Accordingly, before any further pricing flexibility is adopted for the price cap LECs, CCTA asserts that the LEC must certify to the Commission that the following milestones have been attained:

- **Interconnection:**
  - Central office interconnection arrangements must be provided, within 30 days of the date of the Commission's order in this proceeding, to competitive carriers that have requested interconnection. Other competitive carriers must be provided interconnection arrangements within 30 days of the date on which they request interconnection.
  - The specified LEC interconnection must meet the following general criteria: LECs and competitive carriers must be physically interconnected, and competitive carriers must be seamlessly integrated into LEC interoffice and signalling networks, without unnecessary costs or inefficiencies imposed upon the competitive carriers.
  - Establishment of "meet point billing" agreements must be completed, by the same dates, to ensure cooperative economic interconnections as part of the physical interconnection process. The agreements must address the terms and conditions for: the joint provisioning of traffic to interexchange carriers ("IXCs") and the sharing of revenue associated with the completion of 800-

[16] The Commission should also factor into its consideration of the appropriate level of pricing flexibility for price cap LECs, other factors that impact the degree of competition in the marketplace. For instance, for the Tier 1 LECs, the cost of capital is far lower than it is for their potential competitors.

type traffic, calls to information providers, and calls to other providers who bill their customers and pay the LEC for calls, e.g., certain cellular and wireless arrangements.

- Timely provisioning of interconnection trunks must occur in no more than five days where facilities are available.

- **Unbundling and Rights of Way:**

  - As an interim measure as facilities-based competition is being established, the LECs must offer nondiscriminatory access by competitive carriers to unbundled LEC loops, i.e., the complete line to the customer's premises minus the access port, shall be provided within five days of request.

  - Competitive carriers must have nondiscriminatory access to LECs' rights of way, poles, conduit and access points into buildings.

- **Compensation:**

  - A bill and keep methodology of compensation must be adopted, at least until permanent number portability is in place.

  - After such time as permanent number portability is implemented, if the Commission desires to retain bill and keep, there must first be a six month study to determine the balance of traffic. In the event there is not a balance that continues for a six month test period, additional forms of net compensation can be considered.

  - If there is a charge related to the transit function for the use of the tandems, it must be imposed at the LECs' TSLRIC. Moreover, if the Commission decides not to retain bill and keep, then any charges should likewise be based on the LECs' TSLRIC after a six-month study to determine any net imbalance. The integrity of these cost studies is essential to assure the economic viability of local telecommunications competition.

  - Switched access revenue for toll calls terminated by IXCs to competitive carriers' customers prior to the implementation of true service provider number portability shall be transferred by the collecting LEC to the competitive carrier.

- **Number Portability and Numbering Resources:**

  - Equal rights to and control over number resources and no charge for code openings is a necessary prerequisite for effective competition to be possible.

Nondiscrimination in code assignment must be assured and a neutral administrator must be chosen.

- No area code overlays or lack of dialing parity until permanent number portability is fully implemented.

- Implementation of permanent number portability in every LEC central office.[17]

- **Access to Directory Assistance, 911, and Other Databases:**

  - There must be equal status and control of network databases through the use of efficient electronic interfaces available to competitive carriers to access E911, directory listings, directory assistance, line information database ("LIDB"), Signalling System 7 ("SS7") and the other databases necessary for local exchange competition. The LECs must implement provision of these interfaces and provide access within 30 days of the date of the Commission's order in this proceeding, with electronic interfaces up and working within 60 days of the date of the Commission's order in this proceeding, if manual entry is possible in the interim.

The attainment of the foregoing is crucial if facilities-based local telecommunications services competition is to develop beyond the incipient stage. Indeed, requiring the LECs' compliance with these criteria is essential to develop competition in the marketplace to the point where the "substantial competition" test associated with streamlined regulation might ultimately be met.

Moreover, it must be stressed that it is not enough to deem resale-based competition a sufficient basis to proceed with LEC regulatory flexibility. Resale competition is, in fact, nothing more than the sale of the incumbents' underlying service. While providing some limited benefits, such as conditioning the market for competition, it does not offer the full

[17] See Comments of CCTA, CC Docket No. 95-116, filed Sept. 12, 1995 (number portability).

range of public interests benefits, especially improved services, innovative new offerings, and genuine price competition. These benefits can only be attained through the establishment of facilities-based competition. If the Commission does not require, at a minimum, an affirmative certification by the LEC that the foregoing conditions have been met, the likely result of granting the LECs the type of pricing flexibility contemplated in the Second Further Notice will be to permit them to use their new found regulatory freedoms to keep local telecommunications competitors confined to their market niches or toeholds indefinitely. No effective competition of any sort will evolve, let alone at a level that would justify easing regulation in a more significant manner.

Once the LEC can certify to the Commission that the foregoing competitive criteria have been achieved, the Commission must also institute a "fresh look" policy for a period of one year so as to afford an opportunity to examine anew existing contracts for the provision of local telecommunications services that have been signed within the previous two years. Such a policy is critical to facilitating the development of facilities-based competition and will counter the anticompetitive practices of incumbent LECs as they are currently seeking to bind customers contractually in anticipation of the emergence of competition.

Further, the Commission should require that there be a demonstrable and demonstrated level of competition, as measured by market share, of facilities-based competition prior to affording LECs significant regulatory pricing flexibility. In this regard, the Commission should explain why the fifteen percent effective competition threshold that is applicable to cable pricing flexibility should not apply here.[18/] For, just as cable television

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[18/] See 47 U.S.C.A. § 543(a)(2) and § 543(l)(1) (West Supp. 1995).

companies are clearly facing emerging competition from numerous market entrants, including the local telephone companies, there has been a determination that fifteen percent market share is the proper benchmark for deeming a market effectively competitive.[19] Similarly, unless there is clear and convincing evidence that the same threshold should not apply here, principles of fairness dictate the same treatment as competitors enter the local telecommunications services market.[20]

II. THERE IS NO EVIDENCE OF SUFFICIENT FACILITIES-BASED COMPETITION TO FORM THE BASIS FOR THE PROPOSED PRICE CAP CHANGES

A. The Mere Emergence of Competition Is an Insufficient Basis to Alter Service Baskets or Eliminate Lower Service Bands

In March of this year, the Commission issued an order adopting interim LEC price cap rules that the Commission touted as adaptable to competitive market developments for particular services.[21] The Commission further stated that its interim rules "should encourage LECs to make economic decisions that they would make if their markets were

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[19] It should be noted that although certain of cable operators' prices are deregulated when there is effective competition, under the 1992 Cable Act, even a finding of "effective competition" does not end many aspects of rate regulation, such as tier buy-through and uniform pricing requirements. See 47 U.S.C.A. § 543(b)(8)(A) and § 543(d) (West Supp. 1995).

[20] While the Commission does seek comment on possible future streamlined regulation for the price cap LECs, Second Further Notice at ¶ 127, CCTA strongly believes that it is wholly premature to consider such hypothetical regulatory treatment at this time, as it serves only to divert limited resources away from the real issue in this proceeding -- the development of robust facilities-based competition. If and when the fifteen percent threshold is reached, the FCC will have ample time to adapt its regulatory scheme to the then-existing framework.

[21] Price Cap Performance Review for Local Exchange Carriers, First report and Order, CC Docket No. 94-1, 10 FCC Rcd. 8962 (1995) (First Report and Order) at ¶ 4.

competitive."[22] Now, just over eight months after adopting interim price cap rules that give the LECs significant flexibility to adjust their prices in response to competitive entry, the Second Further Notice proposes long term price cap rules that would increase that flexibility to a much greater degree, while dramatically limiting the ability of the Commission, as well as other market participants, to intercede in a timely fashion on behalf of consumers and LEC competitors.

CCTA believes that the adoption of many of the Commission's core proposals will have precisely the effect that the Commission states that it wishes to avoid:

> relax[ing] regulation so much that consumers will be harmed by monopoly pricing or allow[ing] LECs so much pricing flexibility that they could recoup foregone revenues from more competitive services with revenues from less competitive services, or engag[ing] in predatory pricing, unlawful discrimination, or other anticompetitive practices.[23]

The Second Further Notice hails the Commission's proposed price cap plan modifications as facilitating more efficient pricing by LECs and removing incentives for inefficient market entry, as well as encouraging the LECs to introduce innovative services more expeditiously and move their prices closer to their costs.[24] The Commission acknowledges in the Second Further Notice that a competitive marketplace will result in the need for reduced regulation, and in fact champions competition as the ultimate replacement for regulation.[25] Yet, rather than waiting for competition to develop to the degree

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[22] First Report and Order, 10 FCC Rcd at 8967.

[23] Second Further Notice at ¶ 37.

[24] <u>Id.</u> at ¶¶ 34, 37.

[25] <u>Id.</u> at ¶ 18.

necessary to justify greatly reduced regulation, the Commission now proposes to make price cap changes effective "without regard to the current level of competition."[26]

As the Commission is aware, but does not discuss in the Second Further Notice, even in the services and markets where they have made great strides, competitive local service providers have secured only a minute share of the local telecommunications services market. Moreover, even where some inroads have been made, the fact is that facilities-based competition is little more than a concept in danger of being still-born by early deregulation of the LECs. Thus, while total annual revenues in the local telecommunications marketplace are generally estimated to be in the range of $90 billion, total revenues for LEC competitors are expected to be in the range of $1.2 billion for 1995, when all components of the local telecommunications service market are combined.[27] Another indicator of the continued dominance of the LECs in the local exchange market is reflected in the number of access lines that such carriers control. Despite having several hundred networks operational or under construction, competitive carriers account for only a miniscule percentage of the total

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[26] Id. at ¶ 2.

[27] ALTS Members Plan for Massive Growth; Focus Shifts to Marketing, Partnering Opportunities, Telecommunications Reports, Nov. 6, 1995, at 1 (quoting Heather Gold, President of Association for Local Telecommunications Services). In California, with the exception of private line and high speed data services, local only competition has been prohibited since June 13, 1984. See, e.g., CCTA Reply to Pacific Bell's Opposition to Petitions to Deny, File Nos. W-P-C 6913-6916, at Exhibit 1, 11-13 (filed March 11, 1994); California Public Utilities Commission, Enhancing California's Competitive Strength: A Strategy for Telecommunications Infrastructure, Report to the Governor, at 13-15 November, 1993. Toll competition only was made legal on January 1, 1995. Local competition will only begin to exist when the CPUC implements its pending order. Thus, today there is no competition in the local exchange markets.

number of access lines deployed nationwide. Clearly, the tiny percentage of the local telecommunications market that LEC competitors have captured, while certainly a sure sign of emerging competition, hardly amounts to robust competition, and nowhere near approaches the sort of competitive encroachment on LEC markets that justifies the degree of relaxed regulation contemplated by the Second Further Notice.

Significantly, the lack of market share of any facilities-based local service competitors is illustrative of the continued overwhelming market power that LECs still exert today.[28] Given the complete market dominance that the LECs have in the local services market, it would be foolhardy to rely now upon the potential presence of emerging competitors to provide a competitive check on the ability of the LECs to act in an anticompetitive manner. If competition ever is to replace the need for regulation, the emerging market share attained by competitive service providers must translate into a firmly established position. Furthermore, this established position must be measured by reference to a demonstrated market position, such as the fifteen percent effective competition threshold faced by cable television operators,[29] rather than by reference to a fixed date in the future. A future "date certain" for regulatory relief only provides LECs with an affirmative incentive to delay measures that promote local services competition.

Critically, in seeking comment on the need for changes in the price cap service basket structure adopted in 1990,[30] the Commission notes that, at the time of the First Report and

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[28] See Dennis W. Carlton and Jeffrey M. Perloff, Modern Industrial Organization (Harper Collins, 1990), pp. 737-742.

[29] See 47 U.S.C.A. § 543(a)(2) and § 543(l)(1) (West Supp. 1995).

[30] Second Further Notice at ¶ 90; see LEC Price Cap Order, 5 FCC Rcd at 6810-6814.

Order earlier this year, information in the record did not support making any changes in the composition of service baskets.[31] At that time, the Commission stated that a limited increase in downward pricing flexibility would significantly increase the risk of successful predation by the LECs[32] and that it would be premature to modify further price cap baskets and bands because there was a lack of concrete and detailed information about the state of competition and there were no reliable standards for assessing competitiveness.[33] Now, however, the Commission states that as competition emerges for particular services, adjustments may be required in the service basket structure,[34] and that the lower service bands also may need to be eliminated since the accompanying administrative process is so burdensome that it inhibits price reductions.[35]

CCTA concurs with the Commission that changes in the price cap plan service baskets should be linked directly to competition for basketed services. As the Commission has found, the subdivision of LEC services into baskets currently provides needed protection against the LECs' ability to engage in unlawful cost shifting between broad groups of services.[36] Further, the grouping of similar services together in service categories within

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[31] Second Further Notice at ¶¶ 89-90.

[32] First Report and Order, 10 FCC Rcd at 9139-9140.

[33] Id. at 9142.

[34] Id. In this regard, CCTA supported fully the Commission's actions establishing a separate video dialtone price cap basket. See Comments of CCTA, Docket 94-1, filed April 17, 1995 and Reply Comments of CCTA, filed May 17, 1995, (video dialtone price caps basket).

[35] Id. at ¶ 83.

[36] LEC Price Cap Order, 5 FCC Rcd. at 6811.

baskets acts as an added deterrent to anticompetitive behavior by the LECs.[37] As the Commission itself noted, entry barriers remain that impede the development of competition in the local exchange and that require maintaining the current multiple service basket structure.[38] Until there develops genuine facilities-based competition, additional flexibility through changes in the service basket structure will likely impede the progress of competition to the disadvantage of LEC competitors and, thereby, LEC ratepayers. In the long run, CCTA expects that there will exist competition sufficient to act as an effective check on LEC behavior, and multiple service baskets may be eliminated completely. There simply has not been any dramatic change in the level and pace of local exchange competition in the last eight months, however, that would warrant a Commission determination to make changes in the service basket structure at the present time.

Likewise, despite the fact that it cites to no additional evidence as to the existence of meaningful facilities-based competition, and has not set standards for measuring competition, the Commission now proposes not merely to lower the LECs' lower service band limits, but to eliminate them completely. Whereas only eight months ago, the Commission did not possess sufficient information to allow more than a limited increase in downward pricing flexibility, and felt it prudent to retain a requirement that below-band rate reductions be accompanied by cost support,[39] it now proposes to remove completely the lower price band

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[37] Id.

[38] Second Further Notice at ¶ 90.

[39] First Report and Order, 10 FCC Rcd at 9140.

limit and, with it, the requirement that a LEC justify any rate decreases with a showing that the service is priced at or above cost.

The Commission attempts to justify eliminating of the lower service band limit on the myth that such elimination will facilitate the LEC's ability "to engage in true competition."[40] In support of its proposals, the Second Further Notice cites to instances in which the Commission already has allowed LECs to put into effect below-band rates.[41] Therefore, despite the continuing risk of predatory pricing by incumbent LECs, the Commission has concluded arbitrarily that the LECs should have additional pricing flexibility by eliminating the lower service band limits.[42] While the Commission points to the tariff filing or formal complaint process as avenues that remain available for challenging instances of below cost pricing,[43] the truth is that these potential after-the-fact remedies are no real substitute for adequate upfront safeguards.

Incredibly, the Commission has simultaneously proposed to eliminate the requirement to provide cost support for LEC rate reductions and to shift the burden of proof to other parties to prove that a LEC has engaged in below-cost pricing.[44] In effect, then, the Commission has rendered opposition to any proposed LEC rate decreases almost impossible. If the Commission wants to rely on outside parties to detect and uncover abuses, parties must

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[40] Second Further Notice at ¶ 83.

[41] Id. at ¶ 82.

[42] Id. at ¶ 83.

[43] Id.

[44] Id.

be given access to cost support data, the only means to demonstrate that rate decreases are contrary to the public interest. Otherwise, the Commission is all but authorizing any rates the LEC selects with no mechanism to ensure that they are fair and reasonable.

Likewise, the suggestion that the formal complaint process is a satisfactory check on below-cost pricing is wholly irrational and contrary to the public interest. Not only is the formal complaint process at least as administratively burdensome to the parties as a below-band rate investigation is for the LEC, it offers none of the protections of the suspension-and-review process available in a rate investigation.[45] In these circumstances, it is hard to imagine a LEC losing on a complaint of predatory pricing. In fact, the Commission's proposals act to encourage, not discourage, LECs to engage in anti-competitive behavior.[46]

B. LEC Introductions of New Services Require Continued Close Scrutiny By the Commission

The Commission proposes in the Second Further Notice to revise the price cap plan with regard to new service offerings by the LECs because of the Commission's concern that

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[45] Significantly, the Commission's formal complaint process can drag on for years and cause the expenditure of many resources by the parties. For a new and emerging competitor, such a process virtually ensures that any victory, even if ultimately achieved, is hollow as the harm likely has frustrated business plans and successful competition long before.

[46] If the Commission determines nevertheless to adopt additional downward pricing flexibility for the LECs, the lower price band limits should be removed only if the Commission establishes a price floor set at the TSLRIC of the service, plus an appropriate amount of imputed contribution, and detailed cost support must be required. Such rate changes should be allowed only with at least 45 days public notice, to ensure that the outside parties that the Commission relies ever more heavily upon to police LEC behavior actually have an opportunity to provide informed comment. In addition, the LECs, being the entities best situated to provide essential cost data, should bear the burden of proof to show that the proposed rate change is not below-cost.

the current rules may cause delay and may burden the LECs' introduction of new services.[47] In addition to proposing to allow the LECs to introduce new services more aggressively and with less regulatory oversight, the Commission proposes to create a new category of services which, although they are not presently being offered, would nonetheless be exempt from the current regulatory review to which at least some new services would still be subjected.[48] These quasi-new services -- called "alternative pricing plans," or "APPs" -- would be afforded relaxed review.[49] Here too, the Commission proposes to proceed without any evidence of attainable public interest benefits.

The Commission's premise for permitting the institution of optional discounted rates for services that already are offered to some customers is that this will not cause harm to other customers who will have the undiscounted original service still available to them.[50] While this is no doubt true with respect to other users of the original services upon which the APPs are based, the impact is not the same for other LEC customers to whom those original services are unavailable. Thus, the services that are likely to have an APP component are services that probably are and will continue to be available only to large telecommunications users that have both a high volume demand and the financial ability to take advantage of such discounts. In fact, as APPs are likely to be implemented for services available only to large volume users, most small business and residential users are unlikely to be offered APPs.

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[47] Second Further Notice at ¶ 38.

[48] Id. at ¶ 52.

[49] Id.

[50] Id. at ¶ 60.

Consequently, if the LEC that offers an APP is to make up for lost revenues due to the APP discounts, logically the shortfall must be recouped from the non-users of the targeted service -- residential and small business customers that have neither the demand, nor the financial ability to pay for large volume discounts.

Although the Commission fails to provide information sufficient to explain how it arrives at the conclusion that offering APPs without regulatory review will not result in harm to the LEC customers, the Commission may be relying upon elasticity of demand for the APP to make up for lost revenues due to APP price reductions. In other words, the Commission may expect that increased usage attributable to the APP would, on balance, result in higher revenues, thereby offsetting the costs associated with the APP offering. Yet, the Commission completely fails to supply any evidence to support such an assumption.

Indeed, increased usage is not without costs of its own. Specifically, volume stimulation caused by institution of the APP will logically cause traffic sensitive costs to rise, and that volume stimulation further will deplete available network capacity. Thus, even if demand for the targeted service is elastic, the increased revenue ultimately may be less than the increased cost of offering the optional APP. Unfortunately, if the APP is not treated as a new service with the required cost support showing, it will be impossible to know if the incremental revenue increases will be greater than the resulting higher traffic sensitive costs. In turn, this will make it impossible to know if the LEC is generating the positive net revenues necessary for it to justify economically introduction of the APP without resort to cross-subsidization from small business and residential customers.

In addition, even assuming, arguendo, that elastic demand for a LEC's APP offering resulted in positive net revenues, increased traffic resulting from an APP also likely will have a long term impact on a LEC's non-traffic sensitive or facility costs. Put simply, the higher volume of usage due to the APP naturally will absorb excess network capacity. As discounted pricing stimulates demand, the network must accommodate the resulting higher volume of usage. Ultimately, of course, increased utilization of capacity will result in a need for expanded facilities that can be satisfied only by new construction. This in turn drives up the LEC's indirect costs, which are typically spread across all services, and charged to users of all services. Because a LEC's large customers generally account for a relatively small percentage of a LEC's user population, the burden of indirect costs naturally will fall disproportionately on the customers that are not beneficiaries of a self-selected optional discounted service offering. Since the LEC's large customers that can afford the APP are the only users that benefit from it, the burden imposed by sharing the increased indirect costs resulting from the APP constitutes a subtle form of cross-subsidization.

The cross subsidization problems inherent in allowing LECs to introduce APPs without cost support also arise under the Commission's proposed treatment of new LEC service offerings. The Second Further Notice proposes to allow the price cap LECs to introduce certain new services in an expedited fashion, with less cost support, and on shorter notice than under the Commission's current rules for new services.[51/] These new services would be considered "Track 2" services. All other new services would remain subject to

[51/] Second Further Notice at ¶ 45.

current regulatory requirements, including 45 days' notice, and detailed cost support, and would be known as "Track 1" services.

The only showing that the Commission proposes that LECs be required to make for Track 2 services is a showing that the rates for those services will recover the direct costs of providing the service. The potential cross subsidization problem surfaces, however, at precisely this point. If new competitive service offerings are made under Track 2 regulatory procedures, the LEC will have a natural tendency to assign lower direct costs to the Track 2 service in order to demonstrate more easily that the Track 2 service's rates will cover its direct costs. The LEC then will seek to recover from other customers the larger portion of the direct costs associated with the introduction of the new service. Without the detailed cost support of the current regulatory requirements for new services, the Commission and the LECs' competitors will lack the information necessary to challenge any cost-shifting from competitive services to monopoly services. Accordingly, in the event the Commission does proceed, the public interest demands that the Commission not allow LECs generally to offer APPs, or other volume and term discounts, without detailed cost analyses necessary to ensure that small business and residential customers are not in fact paying the tab for services unavailable to them.

In addition to the above, certain other Commission proposals regarding LEC introduction of new services also raise serious problems. For instance, the Commission proposes to shorten the notice requirement for Track 2 new services from 45 days to 14 days.[52/] The Commission also proposes to shorten the notice requirement for restructured

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[52/] Id. at ¶ 49.